

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

| | | | |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|-----------------------------------------------------------------|-------------------|
| Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other | | Local Government Name City of Battle Creek Loan Funds | County Calhoun |
| Audit Date June 30, 2005 | Opinion Date October 14, 2005 | Date Accountant Report Submitted to State: November 23, 2005 | |

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

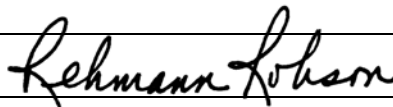
1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- | | |
|---------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

| We have enclosed the following: | Enclosed | To Be Forwarded | Not Required |
|-------------------------------------------------------------------------------|----------|-----------------|--------------|
| The letter of comments and recommendations. | X | | |
| Reports on individual federal financial assistance programs (program audits). | | | X |
| Single Audit Reports (ASLGU). | | | X |

| | | | |
|-------------------------------------------------------------------------------------------------------------|-----------------|-------------|--------------|
| Certified Public Accountant (Firm Name) REHMANN ROBSON GERALD J. DESLOOVER, CPA | | | |
| Street Address 5800 GRATIOT, PO BOX 2025 | City SAGINAW | State MI | Zip 48605 |
| Accountant Signature  | | | |

**CITY OF BATTLE CREEK
LOAN FUNDS ADMINISTERED BY
BATTLE CREEK UNLIMITED, INC.**

Battle Creek, Michigan

Financial Statements

**For the Year Ended
June 30, 2005**



REHMANN ROBSON

Certified Public Accountants

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

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REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



Independent Auditors' Report

October 14, 2005

Honorable Mayor and Members of
the City Commission
City of Battle Creek, Michigan

We have audited the accompanying financial statements of the ***City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc.*** (which consists of an enterprise fund of the City of Battle Creek, Michigan and an enterprise fund of the Battle Creek Downtown Development Authority, a component unit of the City of Battle Creek, Michigan) as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of Battle Creek Unlimited, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. and do not purport to, and do not present fairly the financial position of either the City of Battle Creek, Michigan or the Battle Creek Downtown Development Authority, and the changes in their financial position and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. as of June 30, 2005, and the changes in financial position thereof and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

FINANCIAL STATEMENTS

City of Battle Creek Loan Funds
Administered by Battle Creek Unlimited, Inc.
Statement of Net Assets
June 30, 2005

| | Economic Development Fund | Downtown Development Authority Revolving Loan Fund |
|---------------------------------------------|------------------------------------------|---------------------------------------------------------------------------|
| Assets | | |
| Cash and cash equivalents | \$ 326,422 | \$ 234,224 |
| Investments | 5,814,678 | 258,365 |
| Loans receivable, current portion, net | 794,270 | 19,558 |
| Accrued interest receivable | 37,193 | 3,628 |
| Due from Battle Creek Unlimited, Inc. | - | 1,043,814 |
| Due from DDA Revolving Loan Fund | 245,726 | - |
| | <hr/> | <hr/> |
| Total current assets | 7,218,289 | 1,559,589 |
| | <hr/> | <hr/> |
| Loans receivable, less current portion, net | 5,644,111 | 192,458 |
| | <hr/> | <hr/> |
| Total assets | 12,862,400 | 1,752,047 |
| | <hr/> | <hr/> |
| Liabilities | | |
| Due to Battle Creek Unlimited, Inc. | 3,060,751 | - |
| Due to Economic Development Fund | - | 245,726 |
| | <hr/> | <hr/> |
| Total liabilities | 3,060,751 | 245,726 |
| | <hr/> | <hr/> |
| Net assets | | |
| Unrestricted | \$ 9,801,649 | \$ 1,506,321 |
| | <hr/> <hr/> | <hr/> <hr/> |

The accompanying notes are an integral part of these financial statements.

City of Battle Creek Loan Funds
Administered by Battle Creek Unlimited, Inc.
Statement of Revenue, Expenses
and Changes in Net Assets
For the Year Ended June 30, 2005

| | Economic Development Fund | Downtown Development Authority Revolving Loan Fund |
|--------------------------------|------------------------------------------|---------------------------------------------------------------------------|
| Operating revenues | | |
| Interest on loans | \$ 143,769 | \$ 13,274 |
| Loan fees | 2,960 | 13,027 |
| Other revenue | 33,042 | - |
| | <hr/> | <hr/> |
| Total operating revenues | 179,771 | 26,301 |
| | <hr/> | <hr/> |
| Operating expenses | | |
| Administration | 97,500 | 32,500 |
| Other operating costs | 40,174 | 28,608 |
| Loan loss provision (recovery) | - | (19,698) |
| | <hr/> | <hr/> |
| Total operating expenses | 137,674 | 41,410 |
| | <hr/> | <hr/> |
| Operating income (loss) | 42,097 | (15,109) |
| | <hr/> | <hr/> |
| Nonoperating revenues | | |
| Investment earnings | 150,839 | 10,694 |
| | <hr/> | <hr/> |
| Change in net assets | 192,936 | (4,415) |
| | <hr/> | <hr/> |
| Net assets, beginning of year | 9,608,713 | 1,510,736 |
| | <hr/> | <hr/> |
| Net assets, end of year | <u><u>\$ 9,801,649</u></u> | <u><u>\$ 1,506,321</u></u> |

The accompanying notes are an integral part of these financial statements.

City of Battle Creek Loan Funds
Administered by Battle Creek Unlimited, Inc.
Statement of Cash Flows
For the Year Ended June 30, 2005

| | Economic Development Fund | Downtown Development Authority Revolving Loan Fund |
|--------------------------------------------------------------------------------------------------------------|------------------------------------------|---------------------------------------------------------------------------|
| Cash flows from operating activities | | |
| Loans collected from borrowers | \$ 245,323 | \$ 68,472 |
| Interest and fees on loans | 179,771 | 26,301 |
| Loans made to borrowers and Battle Creek Unlimited | (1,566,513) | (845,666) |
| Administrative and other expense paid | (137,674) | (61,108) |
| | <u>(1,279,093)</u> | <u>(812,001)</u> |
| Net cash used for operating activities | | |
| Cash flows from investing activities | | |
| Purchase of investments | (1,023,993) | (111,023) |
| Proceeds from sale and redemption of investments | 1,715,400 | 99,062 |
| Investment income received | 158,936 | 10,189 |
| | <u>850,343</u> | <u>(1,772)</u> |
| Net cash provided by (used for) investing activities | | |
| Net decrease in cash and cash equivalents | (428,750) | (813,773) |
| Cash and cash equivalents, beginning of year | 755,172 | 1,047,997 |
| Cash and cash equivalents, end of year | <u>\$ 326,422</u> | <u>\$ 234,224</u> |
| Reconciliation of operating income (loss) to net cash used for operating activities | | |
| Operating income (loss) | \$ 42,097 | \$ (15,109) |
| Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities: | | |
| Change in assets and liabilities: | | |
| Loans receivable | (3,904,914) | 48,774 |
| Due to Battle Creek Unlimited | 2,683,724 | - |
| Due from DDA Revolving Loan Fund | (100,000) | - |
| Due to Economic Development Fund | - | 100,000 |
| Due from Battle Creek Unlimited | - | (945,666) |
| | <u>\$ (1,279,093)</u> | <u>\$ (812,001)</u> |
| Net cash used for operating activities | | |

The accompanying notes are an integral part of these financial statements.

CITY OF BATTLE CREEK LOAN FUNDS ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. (the “Loan Funds”) consists of the Economic Development Fund, an enterprise fund of the City of Battle Creek, Michigan (the “City”), and the Downtown Development Authority Revolving Loan Fund, an enterprise fund of the Battle Creek Downtown Development Authority (the “DDA”), a component unit of the City of Battle Creek, Michigan. The Loan Funds provide financing to businesses to create and retain jobs in the City and DDA district, respectively.

The net assets of the Economic Development Fund are the property of the City of Battle Creek; the fund was originally created by an appropriation from the City. The net assets of the Downtown Development Authority Revolving Loan Fund are the property of the DDA; the fund was originally created by a grant received by the DDA from the Miller Foundation. Both the City and DDA contract with Battle Creek Unlimited, Inc. to administer these funds.

The accounting policies of the Loan Funds conform with generally accepted accounting principles as applicable to proprietary funds. A summary of significant accounting policies follows.

Reporting Entity - These financial statements present the financial position, changes in financial position and cash flows of an enterprise fund of the City and an enterprise fund of the DDA; both funds are an integral part of the respective reporting entities. The Loan Funds are not a component unit of the City, DDA or any other reporting entity, as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*.

Basis of Accounting - The Loan Funds are separate accounting entities with self-balancing set of accounts used to report financial position, changes in financial position and cash flows. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain governmental functions and activities.

The Loan Funds are operated as enterprise funds, which are used to account for those operations that are financed and operated in a manner similar to private business or where the governing body has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability. Enterprise funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Loan Funds apply all applicable FASB pronouncements issued through November 30, 1989 in accounting and reporting for their proprietary operations, but have elected not to follow subsequent private-sector guidance.

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The operating revenues of the City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. include interest on loans, loan fees and other revenue. Operating expenses of the enterprise funds include administration, a loan loss provision/recovery and other operating costs. All revenue and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Deposits and Investments – The Loan Funds' cash and cash equivalents consist of demand deposits. Investments are stated at fair value and consist of U.S. treasury notes and other U.S. government obligations.

State statutes authorize local governments to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations, and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

Loans Receivable – Loans receivable consist of balances outstanding from borrowers and are reported net of amounts estimated to be uncollectible.

Net Assets – Restricted net assets represent amounts that are committed for either approved loan applications or minority lending.

2. DEPOSITS AND INVESTMENTS

Deposits – At year-end, the carrying amount of the Economic Development Fund's deposits was \$326,422 and the bank balance was \$326,422. Of the bank balance, \$100,000 was covered by federal depository insurance; the remaining balance of \$226,422 was uninsured and uncollateralized. Also at year-end, the carrying amount of the DDA Revolving Loan Fund's deposits was \$234,224 and the bank balance was \$234,224. Of the bank balance, \$100,000 was covered by federal depository insurance; the remaining balance of \$134,224 was uninsured and uncollateralized.

The government believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the government evaluates each financial institution with which it deposits government funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

At year end, the Loan Funds' investment balances were as follows:

| <u>Category</u> | <u>Fair Value</u> |
|--------------------------|----------------------------|
| U.S. treasuries | \$ 1,487,329 |
| U.S. agencies | 3,994,309 |
| Money market funds | <u>591,405</u> |
| Total investments | <u>\$ 6,073,043</u> |

Credit Risk. All of the Loan Funds' investments in debt securities of U.S. agencies are rated AAA by both Moody's Investor Service and Standard & Poor's. The money market funds were rated Aa3 by Moody's and AA- by Standard & Poor's.

Custodial Credit Risk. For investments, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Loan Funds will not be able to recover the value of their investments or collateral securities that are in the possession of an outside party. Although uninsured and unregistered, the Loan Funds' investments are not exposed to custodial credit risk since the securities are held by the counterparty's trust department in the Loan Funds' name.

Concentration of Credit Risk. At June 30, 2005, the investment portfolio of U.S. agencies was concentrated as follows:

| <u>Investment Type</u> | <u>Issuer</u> | <u>% of Portfolio</u> |
|------------------------|----------------------------------------|---------------------------|
| U.S. agencies | Federal National Mortgage Association | 31.5% |
| | Federal Home Loan Mortgage Association | 10.1% |
| | Federal Home Loan Bank | 21.2% |
| | Federal Farm Credit Bank | 37.2% |

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

Interest Rate Risk. As of June 30, 2005, maturities of the City of Battle Creek's Loan Funds investments in debt securities were as follows:

| | | Investment Maturities (fair value by years) | |
|-----------------|-----------------------|--------------------------------------------------------|---------------------|
| | Fair Value | Less Than 1 | 1-5 |
| U.S. treasuries | \$ 1,487,329 | \$ 49,938 | \$ 1,437,392 |
| U.S. agencies | 3,994,309 | 1,493,175 | 2,501,134 |
| | \$ 5,481,638 | \$ 1,543,113 | \$ 3,938,525 |

None of the U.S. agencies securities are callable.

3. LOANS OUTSTANDING

Loans receivable outstanding as of June 30, 2005, are summarized as follows:

| | Economic Development Fund | DDA Revolving Loan Fund |
|-------------------------------------------------------------|------------------------------------------|----------------------------------------|
| Total loans outstanding | \$ 6,514,182 | \$ 310,016 |
| Allowance for loan losses | 75,801 | 98,000 |
| Net loans outstanding | 6,438,381 | 212,016 |
| Less amounts expected to be collected within one year | 794,270 | 19,558 |
| Amounts expected to be collected beyond one year | \$ 5,644,111 | \$ 192,458 |

Included in the Economic Development Fund's amounts expected to be collected beyond one year are four loans made to Battle Creek Unlimited, Inc. The total amount of these loans is \$3,465,000.

* * * * *



REHMANN ROBSON

Certified Public Accountants

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October 14, 2005

To the Honorable Mayor and City Commissioners
of the City of Battle Creek and the Loan Committee
of Battle Creek Unlimited, Inc.
Battle Creek, Michigan

We have audited the financial statements of the Loan Funds Administered by Battle Creek Unlimited, Inc. for the year ended June 30, 2005, and have issued our report thereon dated October 14, 2005. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America

As stated in our engagement letter dated June 1, 2005, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal control of the Loan Funds Administered by Battle Creek Unlimited, Inc. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Loan Funds Administered by Battle Creek Unlimited, Inc. are described in Note 1 to the financial statements.

As reflected in Note 2 to the financial statements, the Loan Funds Administered by Battle Creek Unlimited, Inc. adopted the provisions of Government Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year fiscal year ended June 30, 2005. The adoption of this new standard had no effect on the financial statements.

We noted no transactions entered into by the Loan Funds Administered by Battle Creek Unlimited, Inc. during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- Management's estimate of the collectability of loans receivable. We evaluated the key assumptions used to develop the allowance for doubtful accounts to determine that they are reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the City's financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by the Loan Funds, either individually or in the aggregate, indicate matters that could have a significant effect on the Loan Funds' financial reporting process.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as [Name of Governmental Unit]'s auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This report is intended solely for the information and use of the Loan Committee and management of the Loan Funds Administered by Battle Creek Unlimited, the State of Michigan, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L'.